

~~CONFIDENTIAL~~

August 5, 1983

ROLE OF U.S. GOVERNMENT GUARANTEE AND TRADE FINANCE PROGRAMS  
IN RESPONDING TO INTERNATIONAL DEBT ISSUES

I. Scope of the Problem

"Successful management of the debt problem will require flexible responses, tailored to the circumstances of the individual cases, among which is:

"encouragement to private markets to provide prudent levels of financing to borrowing countries in the process of implementing IMF-supported adjustment programs"  
NSDD #96, June 9, 1983.

The current debt problems of LDCs are the result of more than a decade of events and policies reflecting, in part, conditions in the industrial market economies, and also weaknesses in their own domestic management. There is clearly a need for concerted international action to maintain both trade and capital flows.

Some LDCs which borrowed heavily -- especially Latin American countries -- are now facing a problem of severe illiquidity, albeit not insolvency. Their ability to service debt depends on:

1. recovery of worldwide demand;
2. a decline in real interest rates;
3. a conscientious effort by LDCs to restructure their domestic economies, through better management; and
4. continued external financing.

Ad hoc debt restructurings will not solve the fundamental problems of some countries. There must be close cooperation between creditor governments, creditor banks, and the IMF to facilitate adjustment over the medium term.

Unfortunately, private banking flows have become much more difficult for LDCs to arrange, and often they are not of a voluntary nature. Most recent data on BIS area commercial bank lending show a very sharp drop between the two halves of 1982 in new lending to Latin America (from \$14.5 to \$4.7 billion at constant exchange rates; in the second half of 1981, new lending to Latin America totaled \$23.3 billion). There was a marked withdrawal of short-term credits.

~~CONFIDENTIAL~~

CONFIDENTIAL

- 2 -

First quarter 1983 BIS data (from a different data base) show a continuing decline in the growth of bank lending, due both to expected seasonal factors (first quarter aggregates normally show relatively little growth) and slower underlying extension of credit; most of the new lending to Latin America in the first quarter went to Mexico and Brazil, in parallel with drawings on the IMF.

The effort of this Working Group has been to examine possible trade financing actions by the U.S. Government, if possible with appropriate burdensharing, to complement established IMF programs. The Group focused on the adequacy of existing U.S. Government programs to respond to extraordinary financing requirements which may arise in some debtor countries by the end of FY 84.

A point to bear in mind is that if additional trade financing is not available from U.S. Government guarantee facilities, the funds required to provide temporary adjustment assistance to major developing country trading partners will either have to come from other sources (possibly from competitors), or the countries concerned will be forced to adjust still further, with concomitant reductions in U.S. exports.

## II. U.S. Strategy

Current U.S. strategy is designed to deal with international debt problems in a flexible manner. It is based on expectations of effective adjustment by the debtor countries, reasonable economic growth in the industrial nations, and an adequate level of financing which allows orderly adjustment and avoids triggering political problems that could damage U.S. interests. There are five elements in this strategy:

1. Primary responsibility must rest with the debtor countries to undertake adequate adjustment measures.
2. The IMF should play a key role in providing official medium-term assistance to troubled borrowers with adjustment programs, and its resources should be increased.
3. Commercial banks must maintain and increase their own lending in the borrowing countries which are following appropriate adjustment programs.
4. Central banks and treasuries must be willing to provide short-term immediate liquidity support, when necessary, to aid selected borrowers which are working out adjustment programs with the IMF.

CONFIDENTIAL

CONFIDENTIAL

- 3 -

5. There must be a resumption of credible economic expansion in the United States, Europe, and Japan. Concomitant to this, protectionism must be avoided so that LDCs can find export markets for their products.

The first phase of the international debt problem has in general been successfully contained. Nevertheless, major difficulties must be anticipated since some LDCs will continue to experience extraordinary liquidity problems. Complex U.S. policy choices -- perhaps even establishing new precedents in some cases -- may be required.

As noted, commercial banks have been reluctant to maintain or increase exposure in many countries. There is uncertainty about the conditions that Congress will impose as the price for authorizing the U.S. share of the IMF's proposed quota increase. Congressional proposals to impose onerous reserve requirements on overdue debt may add additional impediments to international commercial lending.

Developments in debtor countries also add to the uncertainties. There are some (e.g., Brazil) that have been unable to maintain compliance with IMF program conditionality. There are also periodic calls (led by Venezuela) for some form of unilateral debt write-down by a group of debtors.

The combination of internal adjustment and loss of commercial financing, both from banks and directly from commercial suppliers, has caused a sizeable contraction of debtor countries' imports and consequently of U.S. exports. While this statement must be seen in context (in some cases IMF programs have increased imports from sharply reduced levels), the overall impact in many LDC markets has been a decline in imports from major industrial countries from their previous unsustainable levels.

It appears that official lenders will be called upon to provide a larger relative proportion of total finance to LDCs than in previous years.

A. Previous SIG-IEP Review

These issues were examined at considerable length in the SIG-IEP review of the U.S. Approach to the International Debt Problem (NSSD 3-83). The review considered that "adapting the current strategy to changing circumstances is the best way to proceed" in the evolving economic and political situation.

"In view of these uncertainties and the large U.S. economic, political, and security interests at stake, the United States, in cooperation with other major industrial countries, needs to

CONFIDENTIAL

CONFIDENTIAL

- 4 -

closely monitor evolution of the international debt problem. The operation of the strategy in the near term is likely to be turbulent. It should be assessed on a continuing basis, and adaptations made flexibly in light of specific problems, in the framework of the basic approach...." (NSSD 3-83; pp. ii-iii.)

NSDD-96, which the President approved, mandated that an IG-IEP would explore, inter alia:

"The adequacy of U.S. resources for short-term bridge financing and the extent to which multilateral efforts can be expected; and the appropriate use of Exchange Stabilization Fund, Export-Import Bank and Commodity Credit Corporation funds in providing financing to countries of varying importance to U.S. interests.

"The availability of private lending and the adequacy of trade finance facilities -- particularly developments in supplier credits, bank cover and trade receivables; whether improvements can be made in secondary markets for trade paper (i.e., discounting of trade receivables); and whether Export-Import Bank, FCIA and private insurers can play a greater role in facilitating short-term trade transactions."

#### B. The Special Role of Government Guarantee and Trade Finance Programs

The current exercise on the role of U.S. Government programs in managing the debt problems focuses on trade finance and exports rather than on the immediate short-term Treasury and Federal Reserve bridge financing necessary to enable a borrower to remain viable until it can negotiate an IMF program. Trade finance programs can help develop market confidence, promote additional commercial bank lending, check the decline of U.S. exports resulting from debt problems, and facilitate LDC adjustment efforts. It focuses on the exceptional use of such programs in debtor countries experiencing major liquidity problems. In considering programs to finance U.S. exports, a distinction is made between:

- countries which are unable to obtain financing from any source, whereby U.S. guarantees would help the borrower to maintain critical imports from the United States and to maintain the LDC's own exports (i.e., keeping the client alive); and
- providing financing to a borrowing country that it could obtain from another source if not available from the

CONFIDENTIAL

CONFIDENTIAL

- 5 -

United States (i.e., financing in order not to lose market share).

C. Parameters of the Study

(1) The objective of the study is to determine the appropriate role of U.S. Government export credit programs in responding to the debt crisis and then to assess the adequacy of existing programs and funding levels, particularly those of CCC and Eximbank, to deal with the problem. The time frame under consideration is now until end-1984. The review:

(a) emphasizes ways to build on existing programs and to improve their effectiveness in extraordinary circumstances rather than creating new programs or budgeting more resources;

(b) assesses various ways to allocate resources;

(c) analyzes the costs and benefits of any proposed increase in resources.

(2) The purpose is to recommend only the minimum allocations necessary to address debt problems. We propose neither to "throw money" at the problems nor to recommend new export promotion programs. Moreover, it is recognized that extraordinary trade finance support may be related to other measures the U.S. Government might consider to assist a recipient country in managing its overall liquidity and debt problems.

(3) Within the context of the existing strategy, the aim of this study is to develop an approach to assist LDCs with adjustment programs, rather than relieving them of the burden of such programs or removing the disciplinary pressures involved.

(4) The study starts with the premise that the use of official export support programs (and any increase in funding levels) will be designed to catalyze private sector financing and U.S. exports, rather than relieve bankers and exporters of reasonable and appropriate levels of risk.

(5) The aim of the study is not to create longer term "entitlement" programs for LDCs and U.S. exporters; there will be sunset-review provisions included in whatever recommendations are made.

D. What Triggers a Program, How Is It Shaped?

Existence of an IMF adjustment program is generally considered sufficient presumption that an extraordinary trade-financing program could be established. The fact that an IMF program is

CONFIDENTIAL

CONFIDENTIAL

- 6 -

in place is an indication that a country has been experiencing a deteriorating economic situation, possibly a liquidity crisis, and has required and met the conditions for an IMF adjustment program. The specifics of individual situations will differ; i.e., delayed payments resulting from leads and lags, foreign exchange receipts and reserves that do not cover imports of basic commodities and debt service, reserves of less than three months' imports, or cash flow insufficient to sustain minimal levels of international trade.

It is unlikely that the United States would approve a request for extraordinary trade financing assistance without establishment by the borrower of an IMF program (i.e., adjusting on its own) and/or without successful maintenance of IMF conditionality requirements. There must be a presumption against this possibility.

The actual shape of the extraordinary U.S. trade financing program, its contents, and the respective roles of CCC and Eximbank will depend on the specific needs of the borrower and the objectives that the U.S. Government is attempting to achieve. These could, inter alia, entail providing foreign exchange and liquidity; for the demonstration impact on financial market confidence; for assistance in meeting a temporary liquidity runoff which could precipitate a more serious cutoff in financing, attempting to induce commercial banks and trade suppliers to provide more unguaranteed credit than they otherwise would; or to sustain U.S. trade with recipient countries. Other objectives could include assuring the availability of vital inputs necessary for exports, sustaining particular crucial product sectors such as fertilizers; or attempting to insure that foreign private sector firms as well as parastatal enterprises receive a fair share of available foreign exchange resources.

#### E. Burdensharing

Some judgments are necessary on: the appropriate degree of burdensharing with other major countries (especially in the framework of Eximbank programs); the ability of other creditor countries to respond; how strongly WG recommendations can be advanced in the absence of agreement on such burdensharing, and what the U.S. position should be if export financing agencies of other countries refuse to cooperate.

#### F. Creditworthiness - Are We Going to Get Paid Back?

Some of the countries in which CCC and Eximbank have a large exposure are experiencing serious financial problems and may have difficulty in making repayments in a timely manner. Moreover, the existence of an IMF program and meeting its targets could be taken as a good faith indication that the borrower is

CONFIDENTIAL

CONFIDENTIAL

- 7 -

making a genuine effort to redress its economic situation, and thus is creditworthy.

For example, during FY 84, the following countries, which we anticipate will continue to need both normal and possibly extraordinary levels of official financing support, may encounter new or further repayment problems: Argentina, Brazil, Chile, Egypt, Mexico, Morocco, Nigeria, Peru, Philippines, Poland, Sudan, Venezuela, Yugoslavia, and Zaire. (See Table 1, p. 14, most recent Treasury watch list.) What changes, if any, should be made to traditional creditworthiness criteria in responding to these extraordinary circumstances?

#### G. WG-IEP Findings

In determining the appropriate role for the credit and guarantee programs of CCC, Eximbank and other U.S. Government agencies in responding to the debt crisis, the following topics are addressed:

- Should these programs be used to aid countries which are having financing difficulties and, if so, what level of resources should we commit for this purpose through end-1984?
- What is U.S. policy on other uses of these guarantees (e.g., meeting subsidized EC and other competition), and what level of resources should be devoted to these functions?
- Defining the risks of providing these guarantees to countries with financing problems: what are the potential economic and financial costs to the U.S. Government; should funds be appropriated for a reserve to cover contingent liabilities; what, if any, special problems of creditworthiness might be posed by any of these countries?
- What risks, both of an economic and political nature, would be entailed in not providing these guarantees?
- Should there be linkage in the U.S. programs to satisfactory compliance with IMF adjustment programs?
- The extent to which burdensharing might be considered or encouraged.

The following chapters analyze CCC, Eximbank, and other programs (i.e., the State Department's Economic Support Fund and the DOD Foreign Military Sales Loans). A final chapter includes the WG-IEP's overall policy findings and recommendations, building upon the judgments developed in the text on individual programs.

CONFIDENTIAL

CONFIDENTIAL

- 8 -

## III. Commodity Credit Corporation (CCC)

A. Methodology

The primary purpose of this section is (1) to determine whether and how CCC's GSM-102 Export Credit Guarantee Program should be used to aid countries facing a liquidity crisis which might result in a declining market for traditional U.S. agricultural exports; (2) to determine whether the proposed FY 84 GSM-102 guarantee ceiling is adequate<sup>1</sup> to respond to calls upon it for extraordinary financing resulting from international debt problems; and (3) if not, to estimate the level of additional special resources CCC may need to meet such demands.

This analysis first describes CCC's GSM-102 Export Credit Guarantee program and its use thus far in response to international debt problems. It then focuses on estimating (1) the extent to which demands for CCC guaranteed financing in FY 84 directly linked to debt problems can be accommodated within the existing FY 84 \$3.0 billion guarantee ceiling given other program objectives; and (2) what additional resources might be required. This paper is not intended to explore legitimate goals and uses of CCC guarantees beyond those related to liquidity crises.

B. CCC Charter Authority

The primary purpose of CCC under its Charter is to "stabilize, support and protect farm income and prices, assist in maintenance of balanced and adequate supplies of agricultural commodities and facilitate the orderly distribution of agricultural commodities."

CCC's Charter places few restraints on CCC's activities to promote agricultural exports. In providing CCC with authority to provide credit to promote exports and aid in the development of foreign markets for U.S. agricultural commodities, the CCC Charter gives it broad powers to "determine the character of and the necessity for its obligations and expenditures and the manner in which they shall be incurred, allowed and paid."

The Charter permits CCC maximum flexibility to respond to extraordinary situations, although statutory authority establishing various CCC programs (other than GSM-102) may place limitations on their use.

1/ Since CCC has exhausted its FY 1983 guarantee authority, we can assume that the FY 1983 ceiling is not adequate to meet demands in response to debt problems in the remaining two months of FY 1983 without reprogramming or new authority.

CONFIDENTIAL



## CONFIDENTIAL

- 9 -

C. CCC's GSM-102 Export Credit Guarantee Program1. Program Description and Objectives

The primary role of GSM-102, a commercial export credit guarantee program, is to expand the demand for agricultural products from the United States. The program was established as a replacement to the CCC export credit direct loan program as part of an overall strategy to reduce the dependency of agricultural trade on Federal Assistance and increase the role of private sector financing.

Operational since FY 81, GSM-102 is designed to assist U.S. exporters of agricultural commodities in obtaining financing on credit terms of up to three years by providing a partial U.S. Government guarantee covering all risks, both commercial and political.<sup>2</sup> The interest rate on the credit is fixed by the financing institution and is generally set at a small premium above LIBOR, or on occasion, U.S. Prime.

Risk-sharing is an integral feature of GSM-102 since it protects the commercial quality and the financial integrity of the program. Participating U.S. banks are expected to assume a portion of the risk. The standard guarantee covers 98 percent of principal and up to eight percentage points of interest. CCC is permitted to cover up to 100 percent of principal and interest up to the bond equivalent of the most recent 52-week Treasury bill auction average at the time of application. (In only two instances, Poland and Mexico, has the coverage been increased.)

The primary purpose of GSM-102 guarantee program is to develop and maintain markets for U.S. agricultural exports in those countries where credit is necessary to make a sale.<sup>3</sup> Since commercial trade in agriculture is usually

2/ GSM-102 replaced GSM-101 Export Credit Assurance Program, operative 1979-1981, which only insured against non-commercial risk.

3/ Only nations who have Most Favored Nation status are considered eligible (though countries not accorded such treatment are not legally precluded from participation). However, the Jackson-Vanik amendment of the Trade Act of 1974 does apply. Certain other countries are barred by Executive Order or Department of Commerce regulations (e.g., Vietnam, Cuba).

CONFIDENTIAL

## CONFIDENTIAL

- 10 -

on a cash basis, GSM-102 is targeted to those countries which (1) need financing to purchase agricultural imports, (2) need U.S. Government guarantees to secure commercial financing of their imports, and (3) offer reasonable assurance of repayment. GSM-102 guarantees are also intended to provide U.S. exporters with the means to meet foreign competition financed with officially supported credit.

GSM-102 is not generally intended for use by countries (1) where concessional financing or food aid (e.g., P.L. 480) is more appropriate; or (2) which, in the absence of the program, would purchase U.S. commodities for cash. In practice, this has meant that the recipients of GSM-102 belong to the middle and upper ranks of the LDCs (roughly corresponding to the Category II countries in the Arrangement). Countries which no longer fit the generally agreed per capita GNP requirements for P.L. 480 financing are considered particularly appropriate as are countries whose improved financial position warrants "graduation" from food aid programs.

In FY 83, GSM-102 guarantees were used as part of blended credit packages designed to counter subsidized competition.

## 2. Program Implementation

OMB sets an annual fiscal year ceiling on the amount of guarantees CCC can authorize under GSM-102. Within that ceiling, CCC has full responsibility for developing individual guarantee programs. USDA/FAS identifies countries which offer the best opportunities for expanding U.S. agricultural exports and meet the criteria mentioned above, e.g., market development, foreign competition and creditworthiness. CCC is not required to determine the allocation of its entire guarantee authority (or a large percentage) at the beginning of a fiscal year. Though a global budget, which sets priorities and estimates probable annual demands for guarantees, is prepared for internal use, authorizations are made piecemeal throughout the year.

In establishing annual program levels, CCC does not establish a country limitation schedule. However, it does place a ceiling on the cumulative exposure of individual foreign banks (which are required by CCC to issue an irrevocable letter of credit covering the port value (F.O.B.) of the commodity exported). In effect, this sets an upper boundary on the amount of guarantees that can be extended to any one country, as well as CCC's exposure in that country. However, CCC has discretion to increase these amounts by (1) approving new banks; (2) raising the ceiling on already

CONFIDENTIAL

CONFIDENTIAL

- 11 -

approved banks; (3) requesting a government guarantee which permits individual banks to exceed limitations; or (4) waiving bank limits entirely.

All proposed guarantee transactions above \$4 million and/or having a maturity over 360 days are reviewed by the National Advisory Council on International Monetary and Financial Policies (NAC)<sup>4</sup> chaired by the Treasury Department, to ensure that each guarantee is consistent with U.S. financial and international economic objectives, that the recipient country meets standards of creditworthiness, and that the terms of the transaction are appropriate.

### 3. GSM-102 Response to the International Debt Problems

What is the recent history of using the CCC program to assist other countries facing severe liquidity problems? In response to liquidity crises in several countries this fiscal year, CCC has, among other things: (1) continued to authorize guarantees to traditional GSM-102 customers who are experiencing liquidity problems; (2) in some cases, raised guarantee lines to these traditional customers; (3) inaugurated guarantee programs for several countries, which previously had not required credit or CCC programs, to purchase U.S. agricultural products; and (4) had its guarantee ceiling raised to accommodate such demands.

With interagency approval, the following occurred:

-- CCC authorized \$1 billion of three-year guarantees for Mexico in response to its severe liquidity crunch in August 1982.<sup>5</sup> Mexico, a major purchaser of U.S. agricultural exports, had not previously used CCC's programs. OMB agreed to raise CCC's FY 83 guarantee ceiling by \$1 billion since it could not be accommodated within the existing ceiling without foregoing other anticipated allocations.

Due to the nature and size of this program (\$1 billion exceeded the aggregate amount of credit CCC-approved Mexican banks could guarantee), CCC requested and was given the guarantee of the Mexican government. When the commercial banks refused to participate unless their risk was decreased, CCC

4/ NAC membership consists of Treasury, State, Commerce, Eximbank, IDCA, the Federal Reserve and USTR.

5/ Mexico did not have an IMF program in place at the time, but Mexican agreement to such a program was expected shortly thereafter.

CONFIDENTIAL

## CONFIDENTIAL

- 12 -

agreed, as a special exception, to guarantee 100 percent of principal and the maximum eligible interest.<sup>6</sup>

CCC authorized an additional \$200 million of guarantees to Mexico for FY 83 and \$500 million for FY 84. A request by Treasury to increase the FY 83 amount to Mexico by an additional \$500 million this fiscal year is currently under consideration.

-- In the fall of 1982, CCC authorized \$175 million of guarantees as a portion of the U.S. Government's financial response to Yugoslavia's serious debt problems. This was part of a multilateral financial package put together by the United States and Yugoslavia's other major creditor countries.

-- CCC increased its guarantee program to Peru and Brazil this fiscal year. In the case of Peru, CCC continued to register exports under its guarantee line even after it began to receive notices of nonpayment from commercial banks holding CCC-guaranteed credits and Peru undertook a Paris Club rescheduling.

-- CCC established new programs in Chile and Ecuador, when these countries no longer had foreign exchange available to purchase U.S. agricultural exports.

-- A request for \$150 million of CCC guarantees for Nigeria in light of its deteriorating economic and financial situation was initially rejected by the SIG-IEP. The SIG-IEP decided that repayment was not only unlikely but also that extension of guarantees might encourage Nigeria to postpone coming to terms with the IMF and undertaking necessary economic reforms. Eventually a \$30 million guarantee program was approved for Nigeria for foreign policy reasons, but it was the consensus of the SIG that Nigeria would receive no further guarantees until, at a minimum, it has adopted an IMF-supported adjustment program.

One general aspect of CCC's guarantee program should be noted in any discussion of CCC's response to international debt problems. Because the majority of CCC guarantees have been on three-year terms, there has always been an element of balance of payments support inherent in each GSM-102 transaction.

6/ CCC has raised its guarantee coverage only one other time. Principal coverage was increased to 100 percent and interest coverage was dropped to six percent on guarantee lines for Poland. When banks refused to pick up some of the guarantee line, CCC allowed Poland to prepay its unguaranteed interest, making the transactions virtually risk-free for the banks.

CONFIDENTIAL

CONFIDENTIAL

- 13 -

4. Available Authority for FY 84

CCC's guarantee ceiling for FY 84 has been set at \$3.0 billion, \$500 million greater than the FY 83 ceiling presented in the President's FY 83 budget. However, OMB can change these ceilings during the fiscal year.

OMB increased the FY 83 guarantee ceiling three times since January 1982: (1) by \$300 million in April 1982 in response to a USDA request and claim that it would counter a threat by Congress to authorize an export credit revolving fund; (2) by \$1 billion for Mexico in response to a Treasury request; and (3) by \$1 billion in January 1983 in response to a request by USDA for more blended credit funds.<sup>7</sup>

The FY 84 \$3.0 billion ceiling reflects demands for CCC guarantees - (1) to meet subsidized competition (\$400 million); and (2) to develop, maintain, and expand export markets (\$2.6 billion). In setting this ceiling, OMB did not specifically take into account demand for CCC guarantees to deal with the ongoing problem of illiquidity in many developing countries. However, since many countries which are traditional users of CCC guarantees are those experiencing serious debt problems, the current \$3.0 billion ceiling should be able to accommodate some portion of the demand for CCC guarantees directly related to debt problems.

In trying to estimate demands for CCC guarantees for purposes other than countering subsidized competition and debt problems, it is difficult to determine what might constitute "normal" levels of demand for any one country. First, there is not enough historical experience with the credit guarantee program to determine a "normal" usage level. Second, factors influencing credit guarantee requirements change substantially from one year to the next. Thus, any past level of CCC allocations can only serve as an imprecise guideline in estimating CCC allocations for any future year.

With this caveat in mind, based on previous usage (pre-FY 83) of CCC's program, Treasury estimated that as much as \$940 million of CCC's FY 84 \$3.0 billion budget might, in effect, be used to assure that countries experiencing liquidity problems continue to have access to commercial bank financing.<sup>8</sup>

---

<sup>7/</sup> This does not include direct loan increases totaling \$350 million for blended credits.

<sup>8/</sup> This is a Treasury estimate based on FY 82 authorizations to countries in Categories A and B of Treasury's most recent Watch List. USDA declined to provide us with its preliminary estimates of FY 84 authorizations on a country-by-country basis.

CONFIDENTIAL

CONFIDENTIAL

- 14 -

5. Estimated Demand for Extraordinary CCC Support

In the case of CCC, extraordinary demand might be defined as follows:

- (1) demand for CCC guarantees above past usage by those countries experiencing serious debt problems (For this purpose FY 1982 authorizations might serve as an appropriate benchmark for past usage, since in FY 83 authorization levels reflect to some degree both CCC's response to debt problems and blended credit authorizations.); or
- (2) demand for guarantees by those countries which in the past had not required either financing or CCC guarantees to obtain financing to purchase U.S. agricultural products, but as a result of debt problems, now need CCC guarantees to maintain their agricultural import levels.

An analysis of potential demand for CCC guarantees specifically in response to debt problems, therefore must start by making assumptions about the availability of U.S. commercial bank and nonbank trade finance for agricultural exports. However, in the case of CCC's program, unlike Eximbank's, we are not dealing with exact substitutes, since we are not only discussing availability of financing, but also the repayment terms. Even if bank or supplier credits were still available for U.S. agricultural exports to a country identified as having severe debt problems, such financing would be for 180 days not three years.<sup>9</sup>

Assuming that, for these extraordinary cases, three-year terms would better achieve the objective, then we can also assume that the private sector cannot substitute for CCC's program in these cases. Further, assuming that GSM-102 should still not be used for those countries which, in the best of circumstances, are not appropriate recipients of commercial credit, we can identify a list of countries:

- (1) which will likely experience serious illiquidity problems or undergo rescheduling in FY 84;

9/ The three-year CCC maturity confers a benefit on the borrowing country, since the commodity can be sold immediately and the government has the use of the funds for three years. Or, for example, in the case of cotton or soybeans, an importing country can finance its textile industry or soybean processing plant on three-year CCC credits, since the turnaround time from import to export of finished product can be as short as six months. Of course, CCC guarantees can be extended for as short a time as 180 days, but if the intent of these guarantees is to assist countries experiencing short-term liquidity problems to adjust, three-year terms might seem more appropriate.

CONFIDENTIAL

- 15 -

(2) which will likely require CCC-guaranteed financing to maintain adequate food or commodity imports;

(3) which, as a corollary to number (2), will likely be forced to decrease imports of U.S. agricultural products below "normal" levels, if CCC guarantees are not available; and

(4) for which demand cannot be met within the existing FY 84 ceiling.

The following countries would likely meet the above criteria and could be considered likely candidates for some extraordinary financing in FY 84: Brazil, Chile, Ecuador, Mexico, Peru, Philippines, Nigeria and Yugoslavia. Treasury estimates that these countries might require extraordinary financing in FY 84 of approximately of \$2.4 billion.<sup>10</sup>

CCC exposure (contingent liabilities) to these eight countries is currently \$2.7 billion (See Table 2). This represents 34 percent of total CCC exposure. In FY 84, the guaranteed amounts (principal and interest) due to commercial banks by this group is already \$537.6 million. Exposure might increase next fiscal year by only \$160 million to these eight countries based on past annual authorizations. Adding authorization of extraordinary financing based on Treasury's estimate of potential need might raise exposure to these countries by as much as \$1.8 billion. Increase in exposure to these eight countries must also be viewed in the context of exposure to all highly risky countries (Categories A, B, and C of Treasury's most recent Watch List). Current exposure to this larger group is \$4.1 billion.

<sup>10/</sup> Treasury's estimated figure is based on Table 1, Column 4 (Estimated FY 84 Demand minus FY 82 authorizations) adjusted to take into account Treasury's own analysis of potential extraordinary demand by each of these countries. USDA declined to contribute to the determination of demand for extraordinary CCC financing, since it does not want to classify any of its guarantees as being used for extraordinary purposes relating to international debt problems. Instead, USDA/FAS sticks by its estimate that as much as \$4.8 billion increase in guarantee authority for 1984 (a 160 percent increase) is needed based on its country-by-country analysis of demand for credit. This increase would presumably accommodate what Treasury considers extraordinary financing requirements.

CONFIDENTIAL

- 16 -

Table 1

## CCC Authorization/Exposure Levels

FY 1982-84

U.S. \$ Millions

(1)	(2)	(3)	(4)	(5)	(6)	(7)
		USDA Projected Demand for FY 1984 <sup>1</sup>	(3)-(1) Est. FY 84 minus FY 82	(GSM-102) Cumulative Exposure <sup>2</sup>	CCC-Guaranteed Credits Due Banks in FY 84 Principal	Interest
FY 1982	FY 1983					
Auth.	Auth.					
Brazil	355	410	140	893.9	157.4	25.6
Chile	---	138.3	220	16.7	1.1	.3
Ecuador	---	65.3	65	54.5	2.4	.5
Mexico	65	1200.0	1383	1219.5	220.7	3.4
Nigeria	77	30.0	288	---	---	---
Peru	150	178.3	115	337.4	74.8	9.3
Philippines	---	30.0	94	25.1	4.7	.2
Yugoslavia	---	223.0	320	183.6	26.7	4.5
<u>Totals</u>	647	2274.9	2625	2730.7 (348)	487.8	49.8
Total Authorized	2214.6	4730.0				
Total Exposure				8015.7		

1/ This is a rough estimate of demand as opposed to what CCC intends to propose as authorizations.

2/ As of June 30, 1983



CONFIDENTIAL

- 17 -

If CCC continues to make pay-outs, the impact on CCC's total budget will substantially increase.

6. Impact of Reschedulings to Date

Under GSM-102, CCC has paid out claims in three countries; Poland, Sudan, and Romania, totaling \$204 million -- \$142.9 million in FY 81, \$38.4 million in FY 82 and \$22.7 in FY 83.

CCC has not classified any nonpayment under its direct loan program or claims paid to banks under GSM-102 as uncollected losses. The rationale behind this decision is based on CCC's expectation that the funds will eventually be collected. When CCC writes off any of its losses, by statute, additional funds would be appropriated by Congress to enable CCC to repay its outstanding borrowings to the Treasury. Unless and until this occurs, CCC's outstanding borrowing limit -- currently \$25 billion -- is diminished by the amount of funds tied up in unrecovered receivables and reschedulings for which no funds have been appropriated.

CCC includes in its budget a "Contingency Reserve" item to cover unanticipated defaults and nonrepayments of direct and guaranteed loans. This fund, however, applies to all CCC programs. In the 1984 budget this contingency reserve amounts to \$900 million for FY 83 and \$400 million for FY 84.

7. Nonfinancial Risks/Limitations

CCC guarantees cannot be successfully used for emergency bridge financing. However, CCC guarantees can be used as trade financing to help meet the extraordinary financing needs of those countries in which (1) a critical foreign exchange gap exists; (2) a critical food import requirement exists; and (3) commercial banks are unwilling to increase exposure to the extent required.

Given the pressure by the IMF on commercial institutions which has resulted in substantial "involuntary" lending, CCC's credit guarantee program can induce increased levels of bank lending. There are, however, risks and limitations involved in using CCC's guarantee program for such extraordinary financing purposes.

a. Risk-Sharing

If guarantee programs are viewed by the commercial banks as a priority of the U.S. government in responding to debt

CONFIDENTIAL

## CONFIDENTIAL

- 18 -

crises rather than as primarily an export promotion program, it may be difficult to retain risk-sharing in the program. Banks will likely demand 100 percent guarantee cover as was the case with Mexico.<sup>11</sup> This will increase the potential costs of providing extraordinary financing as well as undermine the fundamentals of the entire program.

The U.S. Government should resist this and withstand such pressure. If this is not possible, the SIG-IEP might want to consider cutting out the banks as intermediaries and having CCC lend directly in extraordinary situations. Terms would be commercial -- cost of funds plus a premium to appropriate commercial rates.

The U.S. Government might make some money on its risk, rather than starting a program which completely privatizes the profits and socializes risks. However, this could reinstate the direct loan program, increase budget outlays and would be contrary to the President's Federal Credit Program.

b. Response Time

A guarantee program necessarily relies on the willingness of financial institutions to participate and to take on risk. Though the U.S. Government may be able to authorize a guarantee line immediately, there may be a lag time between authorization and actual use.

c. Country Limitations/Foreign Banks' Ceilings

CCC sets annual country ceilings by limiting the cumulative amount of credit a foreign bank can guarantee. In effect this sets an aggregate limit on the amount of CCC-guaranteed credits any country can have. To overcome this constraint, CCC could approve additional banks or find cause to raise the ceiling of individual foreign banks.

In the case of Mexico, CCC required a Mexican government guarantee. This might be the wisest course of action for all transactions which are viewed as extraordinary, but would require full participating government cooperation.

11/ The banks tried this tactic again regarding programs authorized for Brazil and Chile, but this time their bluff was called. In both countries, the banks have continued to participate in the program.

CONFIDENTIAL

- 19 -

d. Agricultural Importers

An obvious limitation of CCC, which distinguishes it from Eximbank, is that GSM-102 can only be used for those countries which are importers of agricultural commodities. This, of course, precludes its use almost entirely for a country such as Argentina. The most suitable countries for using CCC's program in responding to extraordinary debt situations are countries such as Mexico, Chile, Ecuador, Nigeria, which have large agricultural import requirements and which, in recent years, have been primarily cash purchasers.<sup>12</sup>

e. Trade Policy

Caution should be exercised in carrying out the program to assure minimal adverse impact on foreign exchange earnings of LDCs which export agricultural commodities in competition with the commodities moved under the U.S. program. We compete, for example, with Brazil in soybeans/soybean products; Egypt, Sudan and Pakistan in cotton; and Thailand in corn.

Traditionally, commercial agricultural trade has generally been on a cash/cash-like basis (180-day terms) which corresponds to the economic usefulness of the product. Expansion of this program would, of course, result in greater use of this longer-term credit, i.e., moving away from traditional commercial practice. However, in the current debt situation, this drift away from tradition may already be taking place.<sup>13</sup> Any expansion of this program to respond to extraordinary debt situations should be designed to disappear when the debt situation is improved. Otherwise, this program could further institutionalize the use of credits for products that should sell for cash.

8. Burdensharing

Given the global surplus of agricultural products and competition for markets, creditworthy or otherwise, burdensharing in the agricultural sector is already a reality. That is, we do not need to ask other countries to provide

<sup>12/</sup> OMB believes that the use of guaranteed credit in these cases could substitute for cash sales and conflict with the President's 1984 Budget policy for CCC export credits.

<sup>13/</sup> Agriculture notes that this trend has also been enhanced because of stiff price competition among agricultural exporters.

CONFIDENTIAL

CONFIDENTIAL

- 20 -

officially supported financing for agricultural exports. Nevertheless, in some cases where creditworthiness is in great doubt, bilateral contacts, with Canada and Australia, for example, may be desirable.

9. Policy Framework for Use of Special CCC Resources

a. Any CCC resources earmarked for use in responding to extraordinary debt situations should be held in reserve subject to a decision by the SIG-IEP (or a group designated by the SIG-IEP) to release them for a specific country. Only at that time would OMB be permitted to increase CCC's guarantee authority by the amount of the authorization.

b. A specific, but flexible, set of criteria should be met before extraordinary guarantee lines are authorized. These should be tailored to individual country circumstances, but might include the following provisions:

(i) the borrowing country is currently in compliance with an IMF stabilization program and continues to stay in compliance with it;

(ii) there is continued commercial bank financing. Specifically, guarantees might be used as an incentive for commercial banks to participate in their fair share in new lending to the country in question;

(iii) other governments are providing new credits (not necessarily for agricultural exports) along with the increase in U.S. credits to assure equitable sharing of the financing burden;

(iv) CCC obtains a full faith and credit guarantee of the foreign government; and

(v) any pending or impending debt rescheduling arrangements must form an integral part of such assistance.

c. There should be adequate justification of the decline in agricultural exports that might otherwise result if extraordinary financing were not made available.

d. CCC actions should be coordinated with those of other agencies such as Treasury, State, Agriculture, and AID which can contribute resources to an integrated U.S. Government approach.

CONFIDENTIAL

- 21 -

#### IV. Eximbank

##### A. Methodology

The focus of this analysis is to determine the adequacy of Eximbank's budget authority for FY 83 and the Administration's requests for FY 84, if the Bank is called upon to provide extraordinary financing in response to the international debt problem. For the purpose of this section, extraordinary financing refers to special trade finance facilities established by Eximbank as part of a broader package of U.S. Government and international relief efforts for a country experiencing a severe liquidity crisis.

The analysis will first describe Eximbank programs and its response thus far to the debt problem. Second, this section will evaluate alternative mechanisms through which Eximbank could deliver extraordinary financing. Third, this section will estimate demand for "normal" Eximbank financing through the end of FY 84, i.e., the level of Eximbank direct credits required to neutralize foreign export credit subsidies and the level of guarantees and insurance required to cover standard commercial and political risk not directly associated with the debt crisis. On the basis of these estimates, this section calculates the excess budget authority for FY 83 and FY 84 which could be available for extraordinary financing.

To test the sufficiency of available Eximbank authority to assist particular countries, the paper estimates the outer limits of demand for extraordinary Eximbank financing to meet the contingencies arising from trade finance problems through the end of FY 84. Estimated maximum demand for extraordinary Eximbank support will be evaluated under three scenarios: (1) one major debtor country and two medium-sized debtor countries experience severe liquidity problems; (2) two major debtor countries and four medium-sized debtor countries experience severe liquidity problems; and (3) the highly unlikely case that three major debtor countries and six medium-sized countries experience severe liquidity problems. Finally, the paper will recommend a policy framework for establishing these facilities.

This section will evaluate how extraordinary Eximbank support can respond to liquidity problems by providing not only trade finance, but how such support might be leveraged into additional liquidity support. This section paper does not attempt to detail other measures available to deal with a country's debt problems, such as special liquidity support through the commercial banks, IMF, IBRD, BIS, ESF, and rescheduling. However, it does recognize possible linkages between extraordinary Eximbank financing and these other responses to liquidity problems.

CONFIDENTIAL

## CONFIDENTIAL

- 22 -

The rationale for extraordinary trade finance support is threefold: (1) the provision of special trade finance alleviates the liquidity problem by assuring financing for priority imports and decreasing the drain on foreign exchange available to the borrowing country from other sources; (2) special trade finance could be structured to generate additional liquidity relief, particularly if access to the facilities is conditional; and (3) special trade finance could help support exports to a developing country, which might otherwise be disrupted by lack of credit.

#### B. Eximbank Charter Authority

The primary purpose of Eximbank under its charter is to aid in financing and to facilitate U.S. exports. The charter emphasizes that Eximbank should provide financing for U.S. exports competitive with financing offered by other governments. The charter further stipulates that Eximbank's loans must generally be for specific purposes and must have "reasonable assurance of repayment."

The charter is sufficiently broad to allow Eximbank to be used for contingencies which could arise from LDC debt problems. The charter would not prohibit the Bank from (1) drawing on existing programs; (2) tailoring existing programs to respond to debt problems; or even (3) establishing new programs, if necessary, provided that the financing supports U.S. exports and offers "reasonable assurance of repayment." To the extent that special programs or large amounts of extraordinary financing would be required to meet the debt problem, it would be essential for the Administration to consult with key members of Congress before implementing any special actions.

#### C. Existing Eximbank Programs

Eximbank's buyer credit or project financing window provides long-term financing in the form of either direct loans at fixed interest rates and five- to ten-year repayment terms, as well as financial guarantees of private source loans for heavy capital equipment and capital intensive projects:

-- Direct credits are "targeted" to where the need is greatest to neutralize foreign, officially-supported, subsidized export credits.

-- The terms (interest rates, repayment term, cover) of officially supported export credits are governed by the OECD Arrangement on Export Credits and the Berne Union. At the present time, Eximbank's interest rates and repayment terms precisely match the terms of the Arrangement. The

CONFIDENTIAL

- 23 -

current terms of the Arrangement, however, may change, since a new round of negotiations is scheduled for October, 1983.

-- The convergence of commercial interest rates and the minimum interest rates under the Arrangement has presented an opportunity for Eximbank to make increasing use of its guarantee and insurance programs in the provision of competitive financing.

Eximbank's supplier credit window offers financial support through medium-term commercial bank guarantees, medium-term credits, and short- and medium-term export credit insurance.

-- Eximbank's support for short-term (up to 180 days) export sales has rested exclusively with the export credit insurance program which it has previously operated jointly with the Foreign Credit Insurance Association (FCIA), a group of fifty private U.S. underwriters. Typically, short-term insurance is used for such exports as commodities, raw materials, chemicals, and spare parts.

- The program offers insurance covering commercial and political risks on financing that U.S. exporters and banks extend to their foreign buyers.

- FCIA has covered commercial risk (at 90 percent of principal, interest to maturity date, at the Chase-Manhattan prime rate on date of shipment). As of September 1983, however, FCIA will no longer participate in new Eximbank insurance. Commercial coverage will be for Eximbank's sole risk.

- Eximbank has covered all political risk (100 percent of principal, interest to maturity date, at the Chase-Manhattan prime rate on date of shipment) and has reinsured FCIA commercial coverage beyond specified country and aggregate limits. As of October 1983, FCIA will no longer participate in new Eximbank insurance; all commercial and political coverage for new insurance will be for Eximbank's sole risk.

-- Medium-term insurance policies, previously operated jointly with FCIA, cover exports of capital equipment and other products generally sold on terms of 181 days to five years, with policies written on a case-by-case, seller-to-buyer basis. Such insurance covers capital goods and quasi-capital goods such as power generating equipment, transport equipment, and industrial machinery.

CONFIDENTIAL

CONFIDENTIAL

- 24 -

- Eximbank covers 100 percent of political risk and interest up to the Treasury bill rate plus one percent at time of default.
- Eximbank will assume commercial risk coverage (90 percent of principal, interest up to the Treasury bill rate plus one percent) on all new insurance, as of September, 1983.
- The Bank Guarantee Program offers protection against commercial and political risks on medium-term debt obligations acquired by banks from U.S. exporters. The program covers capital and quasi-capital goods, and insurance coverage is the same as under the medium-term insurance program.
- The Medium-term Credit Program offers fixed-rate medium-term financing under a discount loan program with commercial banks to neutralize foreign, officially supported, subsidized credits.

Generally, Eximbank's Direct Credit Program and Medium-term Credit Program are designed to counter subsidized foreign competition. The Bank's various insurance and guarantee programs, on the other hand, are designed to improve access to commercial export financing by covering the export credit against political and commercial risks.

D. Eximbank's Response to the International Debt Problem to Date

Generally, Eximbank has remained open for business in most markets, even in the face of the international debt problem. Eximbank has taken a country-by-country approach to the issue of determining "reasonable assurance of repayment." The Bank implements specific country policies by specifying conditions for long-term lending under its buyer credit window and adjusting its country limitation schedule for supplier credits.

Some examples of the variety of Eximbank approaches in providing normal financial support (as opposed to extraordinary financing) under existing programs are given below:

- In Chile, Venezuela, Brazil, Peru, and Colombia, Eximbank has stayed open under all programs, but modified the country limitation schedules. At this time, Eximbank's short-term country limitation schedule requires an import certificate from the central government to ensure that the transaction is consistent with the government's efforts to control imports. The Bank also reduced the discretion allowed to U.S. exporters under the short-term and medium-term FCIA insurance programs to \$50,000.

CONFIDENTIAL



CONFIDENTIAL

- 25 -

-- In Argentina, Eximbank has adopted a very restrictive approach in light of continuing public sector arrearages. Nonetheless, Eximbank has continued to honor outstanding credits and commitments for major infrastructure projects, including the hydroelectric project at Yacyreta and a large order of locomotives.

-- In Nigeria, Eximbank has deferred action on new requests for long-term commitments, but has considered extension of existing commitments on a case-by-case basis. Extensions of commitments have been granted for those projects that are revenue-generating, or essential infrastructure such as water resources, power, transportation, and communications. Eximbank has continued to offer short-term and medium-term insurance, but has adjusted the country schedule to require a 360-day waiting period before the holder of the policy can file a claim for transfer risk.

-- In Egypt, Eximbank has followed a cautious policy in which the Bank avoids the large infrastructure projects and large capital equipment transactions more suitable for concessional financing. In general, Eximbank offers support for modest-size projects with potential to earn foreign exchange to service debt. Eximbank requires a government guarantee for transactions involving public sector entities, and the guarantee of a major commercial bank for private sector undertakings.

-- In Turkey, Eximbank has approved a \$200 million limit for new business with the public sector under its operating arrangement with the Ministry of Finance for the coming year. Eximbank remains open for business with the private sector on a case-by-case basis.

-- The Bank has also revised the country limitation schedule for a number of countries in Africa and Central America by reducing discretionary limits and requiring government guarantees.

Eximbank was called upon to provide extraordinary financing in response to Mexico's major liquidity crisis. The Bank established two special \$100 million insurance facilities with major Mexican financial institutions (Nafinsa for public sector borrowing and BNCE for private sector borrowing), as well as increasing the aggregate limit on its insurance facility with Pemex from \$125 million to \$275 million, to cover new sales with short-term or medium-term repayment according to the usual criteria relating to the character of the export. These facilities had the following characteristics:

CONFIDENTIAL

CONFIDENTIAL

- 26 -

-- Eximbank required the full faith and credit guarantee of the Government of Mexico for transactions financed under these facilities. Eximbank insurance and guarantee programs to sovereign public buyers cover 100 percent of principal against political and commercial risk, and a significant portion of the interest rate. This increase in cover transformed foreign risk into U.S. Government risk for the commercial banks engaging in them and effectively circumvented commercial bank exposure limit problems. In addition, an umbrella guarantee allowed Eximbank to show "reasonable assurance of repayment." Eximbank is likely to recover on any claims arising under such a facility.

-- The BNCE and Nafinsa facilities primarily covered short-term (180-day) exports, which theoretically enabled the insurance to be rolled over to cover additional transactions during the year. About one-half of the Pemex facility supported medium-term exports.

-- The facilities allowed maximum flexibility to the Mexican Government in responding to its liquidity problem. The Mexicans could determine the priority products to be covered, as well as which U.S. exporters and banks would have access to the facilities.

-- Some months were involved in putting the facility in place and identifying interested U.S. banks and concluding loan agreements, but once established rapid utilization is expected.

-- Eximbank adjusted its insurance policies to give cover equivalent to an Eximbank financial guarantee. Insurance cover commenced from the time of bank commitment, and cover of interest was extended to include the period from date of default to date of claim payment.

-- Eximbank required documentation at the time of each export to trigger cover under its insurance programs. Documentation ensured that the support was for U.S. exports (legislatively required) and set terms of coverage (which differ depending on type of product and amount of deal).

One key question will be how rapidly these lines can be drawn for specific transactions. Loan agreements with various commercial banks were only concluded by June 1983, and utilization of the facilities has been low to date. Nonetheless, it is expected that the insurance facilities will be rapidly and fully used by the end of CY 1983.

CONFIDENTIAL

CONFIDENTIAL

- 27 -

### E. Mechanisms to Use Excess Eximbank Authority for Debt Problems

Eximbank could deliver extraordinary finance by using either (1) guarantee and insurance authority to establish Mexico-type lines of insured credit; or (2) direct credit authority to provide special facilities for trade finance, which would have immediate balance of payments benefits. Both mechanisms share a number of positive features:

- Each mechanism could help ensure the availability of trade finance and thus help fill financing gaps caused by liquidity problems.
- Each mechanism could be structured to provide additional liquidity support. The debtor country could draw down on the extraordinary direct loans in advance of actual purchases to be used as short-term liquidity financing. Insurance facilities could be used to generate additional liquidity if bank access to the facilities is contingent upon the banks' participating up to their fair share in new lending to each country.
- Both facilities allow maximum flexibility to a debtor government in responding to its debt problems. It can determine the priority products to be covered as well as which U.S. exporters and banks would have access to the facilities.
- Both facilities could be structured to support U.S. exports to the private sector as well as exports to public sector entities.
- Both mechanisms can also be implemented rapidly, although actual disbursements could probably proceed more quickly under special direct credit facilities.
- Under both mechanisms, the U.S. Government could stipulate special conditions or make special exceptions. To the extent that the facilities go beyond normal conditions (i.e., those of the Berne Union and OECD Arrangement on Export Credits), multilateral coordination should be undertaken.

Generally, however, the delivery mechanism for extraordinary Eximbank financing should be through special insurance facilities rather than special direct credit facilities. The major advantages of using insurance facilities are as follows:

- Insurance facilities would draw on existing Eximbank guarantee/insurance authority, consistent with the Administration's Eximbank budget policy to place more emphasis on guarantees and insurance.

CONFIDENTIAL

CONFIDENTIAL

- 28 -

-- Insurance facilities fall within the parameters of current Eximbank insurance and guarantee programs. Insurance coverage would only be triggered when a U.S. export occurs. The insurance programs are already designed as the type of multipurpose lines to support commodities, spare parts, and capital goods which debtor countries require in a liquidity crisis. The proposed direct credit mechanism would require a major shift in U.S. Government policy on the use of direct credits (which are currently targeted against foreign subsidized competition) and a broad interpretation of Eximbank's Charter to permit such loans to be used for interim liquidity finance until the U.S. export goes forward.

-- Insurance facilities would have considerably less budget impact. First, Eximbank has much more excess guarantee and insurance authority (\$2.0 billion in FY 83 and \$3.0 billion in FY 84) than direct credit authority (\$2.0 billion for FY 83 only). This may be adequate program authority to offer special direct credits loans in FY 83, but authorization of such loans during FY 84 would probably require the Administration to request supplemental direct credit authority for FY 84. If excess direct credit authority does exist, use of it in this manner would increase budget outlays and increase the Federal deficit.

-- Insurance facilities could be used to encourage a greater commercial bank role in responding to liquidity problems.

Nonetheless, there may be special circumstances when special direct credit facilities could be used rather than insurance lines, especially those instances when a quicker infusion of funds would provide a demonstrably greater benefit to the debtor country. <sup>14</sup>

Conditionality: The provision of these extraordinary financing facilities should be linked to a number of explicit, but flexible conditions, according to individual country circumstances. These include:

-- The government of the recipient country should provide its full faith and credit guarantee.

-- The facilities should be specifically linked to continued commercial bank financing and might be used as an incentive for commercial banks to participate in their fair share in new lending to each country.

14/ OMB does not believe that Eximbank direct credits are an appropriate mechanism to use to provide a quick infusion of funds. Such short-term liquidity problems are better addressed by mechanisms such as the Exchange Stabilization Fund.

CONFIDENTIAL

CONFIDENTIAL

- 29 -

-- Other governments should provide new credits along with the increase in U.S. credits to assure equitable sharing of the financing burden.

-- The extraordinary credits should be provided only to countries with IMF stabilization programs and which stay in compliance with them.

-- Any pending or impending debt rescheduling arrangements would normally form an integral part of such extraordinary financing.

F. Eximbank Budget Policy

The President submits the Administration's proposed limits on Eximbank's programs and Congress in annual appropriation bills sets limits on Eximbank's (1) direct credit authority, and (2) guarantee and insurance authority for each fiscal year. The Bank cannot legally shift direct credit authority into guarantee/insurance authority (or vice versa) without Congressional approval, but can generally, after consultation with OMB, shift authority among its various guarantee and insurance programs. In terms of the budget, only Eximbank's net direct loan activity (essentially gross loan disbursements minus loan repayments), plus net claims payments on guarantees and insurance, results in outlays and increases the Federal deficits.

For FY 83, the Administration requested \$3.8 billion direct credit authority and \$8.0 billion guarantee and insurance authority. Congress authorized \$4.4 billion in direct credits and \$9.0 billion in guarantees and insurance.

For FY 84, the Administration has requested credit limits of \$3.8 billion in direct loans and \$10.0 billion in guarantees and insurance. In addition, the Administration pledged that it would request supplemental direct credit authority of up to \$2.7 billion, if needed to meet inappropriate foreign subsidized credits.

These requests reflect both the Administration's long-run export credit policy and response to the international debt situation. The level of requested direct loan authority reflects expected economic trends, as well as an effort to increase use of long-term guarantees. The \$10 billion request for insurance and guarantee commitments represents a \$2.0 billion increase over the FY 83 request and is \$4.0 billion more than the Bank authorized in FY 82 and is likely to commit in FY 83.

One major reason for the increase in the FY 84 request for guarantee and insurance authority was to encourage the continued availability of credit for U.S. exports in the face of the ongoing indebtedness problems in developing countries.

CONFIDENTIAL

CONFIDENTIAL

- 30 -

G. Available Authority for FY 83 and FY 84

FY 83 Authority: Eximbank's projections as of June 28, 1983, indicate that it will have considerable program authority available for extraordinary financing through the rest of FY 83. Remaining direct credit authority will amount to at least \$2.0 billion, while remaining guarantees and insurance authority will amount to at least \$2.0 billion. With two months remaining in FY 83, the \$4.0 billion in excess authority should be ample for any contingencies which may arise.

FY 84 Authority: The Administration has requested \$3.8 billion in direct credit authority and \$10.0 billion in guarantee and insurance authority. It is difficult to project exactly how much room there will be for special programs in FY 84, but it is possible to construct rough estimates based on historical levels and projections of U.S. exports (especially capital goods) and the historic ratio of Eximbank activity. The demand for Eximbank resources will be a function of (1) the level of U.S. capital goods exports to developing countries, (2) the interest rate environment in the United States, (3) the interest rate matrix of the Export Credit Arrangement, (4) foreign competition, and (5) the demand for project finance.

(1) Direct Credits. Eximbank direct credits will continue to be targeted against foreign, officially supported, subsidized financing. Demand for Eximbank direct credits to support non-aircraft exports to relatively rich countries will be small, given the current level of commercial interest rates and Arrangement rates for relatively rich countries. Eximbank will continue to offer competitive financing for exports to intermediate and relatively poor countries, as well as competitive aircraft, unless U.S. interest rates drop and/or the new Arrangement ties rates for intermediate and poor countries to market rates.

The demand for Eximbank direct credits for FY 84 is roughly estimated to be no more than \$3.8 billion, the amount which the Administration requested. This estimate is based on the following:

-- The demand for Eximbank support for non-aircraft, non-nuclear capital is estimated at \$2.4 billion for FY 84. This estimate is based on the typical share of capital goods exports supported by Eximbank and Chase and DRI projections that capital goods exports will remain basically flat during FY 83 and FY 84. This estimate is further substantiated by demand estimates based on a forecast of major projects likely to require Eximbank support in FY 84. However, similar forecasts last year overestimated the activity for FY 83; to date, Eximbank has only authorized \$246 million for this category in FY 83.

CONFIDENTIAL

## CONFIDENTIAL

- 31 -

-- The demand for Eximbank support for nuclear projects is very uncertain. Major projects have been forecast in the budget every year since 1980, but have failed to materialize. An estimate of \$250 million is included to account for the low level of FY 84 Eximbank financing expected in possible projects.

-- The demand for Eximbank support for aircraft is estimated at only \$400 million, due to the sluggish recovery of the world economy and the growing capacity of airlines as earlier orders continue to be delivered.

-- Demand for other programs (discount loan and medium-term credit) is expected to rise to \$600 million. The medium-term area is expected to show a quicker recovery than the long-term credits, because of the shorter lead time for importer contract deliveries for such types of equipment.

(2) Guarantees and Insurance: It is more difficult to estimate "normal" demand for guarantees and insurance. Such demand is generally a function of the level of trade and the assessment of risk by exporters and their banks. Decreasing international trade in the past year lowers the demand for insurance while perceptions of increased commercial and political risks (as evidenced by the reduction of supplier credits to high debt developing countries) may increase the share of international trade which is insured.

The following table shows the traditional levels of Eximbank guarantees and insurance:

Guarantees and Insurance Authorizations  
(\$ millions)

FY	Guarantees	Insurance	Total
1978	589	3362	3951
1979	908	4108	5016
1980	2510	5521	8032
1981	1513	5910	7223
1982	727	5105	5832
1983	(estimated)		6300

The demand for Eximbank guarantees and insurance peaked in FY 80, in part because of use of unusually large amounts of financial guarantees as substitutes for limited direct loan authority. Otherwise, the annual demand for guarantees and insurance has been about \$7.0 billion or less.

CONFIDENTIAL

## CONFIDENTIAL

- 32 -

Normal demand for insurance and guarantees in FY 84 is not likely to be above \$7.0 billion:

-- World economic recovery is expected to be sluggish and U.S. trade is not expected to increase to levels significantly greater than in FY 83.

-- Even in FY 83, when Eximbank is providing extraordinary insurance facilities for Mexico and fairly extensive insurance authorizations for countries such as Nigeria, demand for insurance and guarantees is estimated to be less than \$7.0 billion.

-- Those markets in which trade finance is drying up are the most likely candidates for extraordinary financing, rather than normal Eximbank guarantees and insurance. For example, most of the problem debtor countries are in Latin America, which accounts for about 35 percent or \$2.5 billion of the Bank's normal guarantee and insurance authority.

It is likely that Eximbank will have about \$3.0 billion excess guarantee and insurance authority available for extraordinary financing during FY 84.

(3) Excess Eximbank Program Authority through end-FY 84. Eximbank has substantial program authority remaining through the end of FY 84, a total of \$7.0 billion. (See table below.) Guarantee and insurance authority is adequate for extraordinary finance in FY 83 and FY 84, and direct credit authority is adequate for FY 83. If special direct credit facilities are used in FY 84, the Administration may have to request supplemental direct credit authority for FY 84. Any large transactions which use excess FY 83 program authority (\$2.0 billion in insurance and guarantees and \$2.0 billion in direct credits) for extraordinary finance would have to be authorized by the end of August to allow for Congressional review.

Estimated Excess Eximbank Program Authority  
(\$ billions)

<u>Program</u>	<u>FY 83</u>	<u>FY 84</u>	<u>Total</u>
Guarantees and Insurance	2.0	3.0	5.0
Direct Credit	2.0	--	2.0
Total	4.0	3.0	7.0

CONFIDENTIAL



CONFIDENTIAL

- 33 -

H. Demand for Extraordinary Eximbank Support by End of FY 84

It is difficult to estimate the demand for extraordinary Eximbank financing to meet contingencies arising from the debt problems through the end of 1984, particularly since it is not possible to predict with certainty which countries will require extraordinary financing and which countries will not. At best, the maximum demand for extraordinary financing can be evaluated under three scenarios: (1) one major debtor country and two medium-sized debtor countries experience severe liquidity problems; (2) two major debtor countries and four medium-sized debtor countries experience liquidity problems; and (3) three major debtor countries and six medium-sized countries experience liquidity problems.

Individual indicative countries are evaluated in order to get some sense of the order of magnitude of the problem. The criteria for selecting these countries were that they were indicative of developing countries in which U.S. trade and Eximbank exposure are traditionally fairly significant. For purposes of analysis, indicative major debtor countries include Brazil, Korea, Mexico, and Venezuela. Indicative medium-sized countries include Argentina, Chile, Indonesia, Nigeria, Peru, Philippines, and Yugoslavia. It must be emphasized that these lists are only indicative lists; the appearance of any country on this list as well as the analysis that follows does not necessarily mean that the country is having severe liquidity problems which would require extraordinary financing.

A rough method to estimate the outer limits of country demand for extraordinary Eximbank trade financing is to evaluate that country's trade account with the United States. Table 2 summarizes the maximum estimate of extraordinary Eximbank support by country, reflecting 1982 trade patterns and potential eligibility for (1) short-term insurance; and (2) medium-term insurance and guarantees, as well as long-term Eximbank financing.

This analysis is only being used to estimate the largest possible demand which extraordinary financing could put on Eximbank's budget. This analysis is in no way predictive nor by itself should be used to determine specific country allocations. This analysis needs to be considered in the context of the overall availability of capital to a country experiencing severe liquidity crisis before determining specific amounts of extraordinary trade financing to be provided.

Amounts hypothesized are based on a number of assumptions:

-- Short-term insurance is for six months and is assumed to be cycled twice per annum.

## CONFIDENTIAL

ESTIMATE OF THE MAXIMUM DEMAND FOR EXIMBANK EXTRAORDINARY  
FINANCING BY INDICATIVE COUNTRY 1/  
(\$ million)

<u>Country</u>	<u>Maximum Eximbank Support</u>			<u>Authorizations</u>	
	<u>Short-term</u>	<u>Medium-term/ Long-term</u>	<u>Total</u>	<u>FY 82</u>	<u>FY 83 on June 30</u>
<u>Large Debtors</u>					
Brazil	500	500	1000	347	189
Korea	684	742	1426	204	17
Mexico	1377	1795	3172	1376	412
Venezuela	436	1088	1524	545	242
<u>Medium-sized Debtors</u>					
Argentina	134	311	445	659	22
Chile	69	143	212	79	44
Indonesia	179	453	632	430	98
Nigeria	63	233	296	153	44
Peru	75	225	300	198	101
Philippines	229	224	453	73	272
Yugoslavia	81	51	132	103	31

1/ These figures are estimates of the outer limits of demand for Eximbank support for each country, based on evaluations of the U.S. trade account with these countries in 1982. They are not predictions of which countries, if any, may require extraordinary financing. The countries were chosen as representative of developing countries in which U.S. trade and Eximbank exposure are traditionally significant. This table is in no way predictive nor by itself should be used to determine specific country allocations. Country allocations would need to be considered in the context of the overall availability of funds to a country before determining specific amounts of extraordinary financing to be provided.

CONFIDENTIAL

CONFIDENTIAL

- 34 -

-- Hypothetical coverage for most categories is based on an assumed use of Eximbank support for no more than 50 percent of total U.S. export volume. The 50 percent figure is only indicative, but nonetheless based on the view that (1) it would be administratively impossible to mobilize trade finance for most exports under a special facility; and (2) other sources of finance will be mobilized to share the burden in a major liquidity crisis, as they have during 1983.

-- The estimates assume that Eximbank would not support agricultural commodities because of the availability of support from the Commodity Credit Corporation, but Eximbank insurance could be employed also as it has been in the past.

-- Extraordinary finance would only go for priority products. Items such as passenger cars, TV sets, and consumer goods are not included in the estimates.

The table reveals that Mexico could require the most Eximbank support in the context of a major liquidity crisis -- \$3.1 billion, which is about \$1.8 billion more than 1982 Eximbank authorizations. The maximum Eximbank support ranges from \$1.0 to \$1.5 billion in Brazil, Venezuela and Korea, which is about \$500-700 million more than "normal" annual authorizations. For medium-sized countries, maximum extraordinary financing ranges from \$150 million to \$500 million, on average \$100 million more than normal authorizations per country.

These figures may be overestimates because:

-- During Mexico's recent financial crisis, it clearly did not require such huge levels of Eximbank support. Eximbank's special insurance facilities amounted to \$350 million in support. Eximbank estimates that total demands by the end of CY 83 will probably be no more than \$700 million, although Mexico estimates \$900 million.

-- The trade account analysis is based on 1982 trade figures. The 1982 levels of imports for most of these countries were significantly higher than the period 1978-1980 and were only surpassed in 1981.

-- The trade account analysis is inflated by including mineral fuels (which are subject to existing commitments) and crude materials (which may be difficult to finance under a facility because of the diversity of suppliers).

-- It could be difficult for most of these countries to administer and absorb Eximbank support under insurance schemes for such large amounts in a short period of time.

CONFIDENTIAL

CONFIDENTIAL

- 35 -

-- In any major international relief program, other sources of liquidity (IMF, IBRD, foreign exchange earnings, etc.) would be available to support a significant portion of the demand for imports from the United States.

Nonetheless, these figures indicate the following maximum extraordinary financing requirements over and above FY 82 Eximbank authorization levels:

Scenario I: If one major country and two medium-sized countries need extraordinary financing, the absolute maximum additional demand on Eximbank resources would range from \$1.0 billion to \$2.0 billion, depending on whether Mexico was a major country in liquidity crisis.

Scenario II: If two major countries and four medium-sized countries required extraordinary financing, the absolute maximum additional demand on Eximbank resources would range from \$2.0 billion to \$3.0 billion.

Scenario III: If three major countries and six medium-sized countries need extraordinary financing, the absolute maximum additional demand on Eximbank resources would range from \$3.0 to \$3.6 billion.

The Administration will not have to seek additional Eximbank authority for FY 84 in order to cover the most likely contingencies, unless there is a decision to offer direct credits through special direct credit facilities. Since Eximbank will have \$2.0 billion in excess insurance and guarantee capacity for the remainder of FY 83 and is likely to have \$3.0 billion in excess guarantee and insurance authority for FY 84, the Bank should have enough guarantee and insurance authority to cover the need for extraordinary financing through the end of 1984. If special direct credits facilities are used, then the \$2.0 billion in direct credits now available for FY 83 should be sufficient. For FY 84, additional direct credit authority would probably be needed for special direct credit support.

#### I. Policy Framework for Special Eximbank Facilities

(1) Special Eximbank programs should be based on a clear economic rationale, particularly so the Congress can understand it. For example, the Administration should have projections which indicate the magnitude of the gap in import financing available to a country designated to receive the special assistance before determining how much special Eximbank support is needed.

Alternative financing gaps for a particular country could be defined according to different assumptions as to growth rates in that economy and likelihood of various sources of financing.

CONFIDENTIAL

CONFIDENTIAL

- 36 -

In the past, such estimates have varied from reality, so that the special Eximbank programs may not be made on precise projections. Based on reasonable ranges of estimated need, the special programs should be sufficiently large and flexible so as to (1) inject funds quickly; and (2) help instill confidence in private sources of financing to that country.

(2) SIG-IEP should establish criteria which can discriminate among potential recipient countries. The provision of extraordinary financing facilities should be linked to a number of explicit, but flexible, conditions, according to individual country circumstances. These include:

(a) The government of the recipient country should provide its full faith and credit guarantee.

(b) The facilities should be specifically linked to continued commercial bank financing and might be used as an incentive for commercial banks to participate in their fair share in new lending to each country.

(c) Other governments should provide new credits along with the increase in U.S. credits to assure equitable sharing of the financing burden.

(d) The extraordinary credits should be provided only to countries with IMF stabilization programs and which stay in compliance with them.

(e) Any pending or impending debt rescheduling arrangements would normally form an integral part of such extraordinary financing.

(3) The SIG-IEP can develop and require additional conditions and amend existing conditions for the provision of extraordinary financing, either to be generally applied or country-specific.

(4) The SIG-IEP should coordinate the actions of Eximbank and other agencies such as State and Agriculture which can contribute resources to an integrated U.S. Government approach.

(5) The implementation of extraordinary financing facilities may vary dramatically from country to country, since programs should be tailored to particular country requirements. Extraordinary financing facilities would presumably be provided not only to countries experiencing immediate liquidity crises, but to those countries in the process of working their way out of a debt problem as a means of assisting this process. Examples of different objectives which may fall within the context of extraordinary financing and may require varied responses could include:

CONFIDENTIAL

CONFIDENTIAL

- 37 -

(a) Providing liquidity financing that a government can use to provide general foreign exchange needs on the capital and trade accounts.

(b) Building confidence to discourage speculative withdrawals of private credit.

(c) Leveraging private capital by inducing private lenders to provide more unguaranteed credit than they otherwise would.

(d) Sustaining minimum trade flows critical if trade finance is unavailable or scarce.

(e) Assuring the availability of the necessary imported inputs for critical export production.

(6) The Eximbank special actions should be structured toward

(a) demonstrable benefits to sustaining normal U.S. exports; and

(b) "bailing in," not "bailing out," the banks.

(7) Actions to bring in the banks would call for maximum use of Eximbank insurance and guarantees to entice commercial banks and exporters to provide liquidity financing.

(8) In each case, the SIG-IEP and appropriate government agencies should judge whether there is a reasonable assurance of repayment of extraordinary financing. This requirement presumably could be met by making governments the obligors or guarantors, by the conditionality provisions and evidence of parallel actions by other governments, international financial institutions, and private banks, and by evidence that the recipient is taking steps to work its way out of its debt problem.

(9) In the event of a multinational debt rescheduling the issue arises, how should Eximbank's special support efforts be treated? Short-term support efforts might, for example, be rescheduled into a much longer repayment term than originally-intended.

(10) Any extraordinary financing facilities should have a "sunset clause," e.g., direct or guaranteed lines of credit should have an expiry date.

#### J. Implementation Program

Any countries which require extraordinary financing should be identified as soon as possible so that the necessary implementation can proceed. The provision of special facilities should take into account international economic and foreign policy

CONFIDENTIAL

## CONFIDENTIAL

- 38 -

concerns in addition to the debt problems of the recipient country. In order to use Eximbank's FY 83 program authority for these purposes, Eximbank must authorize special facilities in excess of \$100 million by August 25. Disbursements can occur in any subsequent time period, not restricted to any fiscal year. Prior to such authorizations, consultations will be required with the authorities of the recipient countries and the U.S. Congress.

The authorizations can be made subject to the conditions which the Administration may wish to establish now and negotiate later with the recipients and other countries and commercial banks which may be sharing the burden. In addition, the banks which may implement the facilities in the U.S. and the recipient countries may only be identified after further negotiations.

## V. Security Assistance Programs

### A. Economic Support Fund

The Economic Support Fund (the Fund) provides highly concessional loans and grants. Current legislation authorizes the President to furnish Fund assistance "to countries and organizations on such terms and conditions as he may determine in order to promote economic or political stability."

Where the Fund is used in countries facing serious debt problems, there are no obstacles to using it as short-term, fast-disbursing assistance linked to policy reform, IMF programs or other. Since several countries who receive Fund assistance are those with debt problems, some portion of the FY 1984 \$3 billion Fund budget could help address liquidity problems in those countries.

Recent legislative history, however, indicates Congress does not perceive non-project assistance to be a "development" activity, and increased use of the Fund for debt relief could lead to explicit Congressional prohibitions. Moreover, extension of Fund assistance to countries that are not recipients of traditional U.S. bilateral aid could undermine current U.S. development policy (e.g. maturation/ graduation).

### B. Military Assistance Programs

The Foreign Military Sales (FMS) credit programs are large and growing. The interest rates are the cost of money to the U.S. Treasury plus 1/8 percent. These relatively hard loan terms, as well as the large and growing levels of debt incurred by many countries to buy military equipment, are an increasingly significant part of the problem in some debtor countries.

CONFIDENTIAL

CONFIDENTIAL

- 39 -

Section 1 of the Arms Export Control Act mandates that activities undertaken under the Act should not cause undue burden on recipient country economies. This mandate has been used by the Executive Branch as the basis for seeking greater concessionality in FMS programs, e.g. lower interest rates, longer repayment periods, etc.

The security assistance of the United States and its friends and allies will continue to require extension of FMS guarantees and credits, as well as Military Assistance Programs (MAP). To the extent more concessionality can be introduced in FMS programs financed on relatively hard loan terms, it should be actively considered in a separate but related exercise.

#### VI. Burdensharing

Some countries have more flexibility in responding to debt problems in the methods in which relief can be offered, as well as the timing of the response. Therefore, we are gathering intelligence on the programs available and the constraints present in major foreign creditor countries, in order to be in a stronger position when negotiating burdensharing options with other creditor countries.

A country's contribution should be viewed as a total package and not segmented by capital goods, agricultural goods, etc., in an attempt to achieve comparability on a program by program basis. In some instances the United States may respond with both Eximbank and CCC support, while in other instances, solely with one or the other, but in any case it is the total relief which is important.

Once we have a better understanding of the foreign creditor countries' debt relief capabilities and policies, the SIG will be in a better position to discuss and decide on a burdensharing formula to apportion debt relief responsibility among the creditor countries. Such a formula could be based on, for example, a combination of trade patterns and government/bank exposure.

Trade policy factors will have to be addressed in determining a burdensharing formula. For example, if it makes more sense for the United States to offer agricultural support to country x, given our own comparative advantage, would we be putting our share of the capital goods market in that country at risk by allowing a foreign government to capture the market through extraordinary financing? On the other hand, there may be instances of extraordinary financing when we would welcome expanded financing of manufactured goods by other countries and we would do our share by financing agricultural goods.

CONFIDENTIAL



CONFIDENTIAL

- 40 -

VII. Conclusions

Both Eximbank and CCC programs should continue to be used in extending extraordinary financing to respond to the LDC debt crisis. The IMF cannot remedy the LDC debt crisis alone. Creditor country governments and private financial institutions should cooperate with the IMF in providing new credit to countries seeking debt relief.

Capabilities and Constraints. Eximbank and CCC can provide extraordinary finance, either by using guarantee and insurance authority to establish Mexico-type lines of insured/guaranteed credit, or by using direct credit authority, which can each provide balance of payments benefits. Although both the direct credit and guarantee mechanisms can be structured to provide additional liquidity support, it is recommended that extraordinary financing generally be delivered through special insurance facilities.

Where the Economic Support Fund (ESF) is used in countries facing serious debt problems, there are no obstacles to using it as short-term, fast disbursing assistance linked to policy reform or IMF programs. Congress, however, may object to the use of the Fund for debt relief. The Foreign Military Sales programs, which are large and growing, have become part of the debt problem in some debtor countries. The role of these credit programs should be reviewed in a separate, but related exercise.

While Eximbank appears to have adequate guarantee/insurance authority over the FY 83-84 period, CCC is facing budget restraints. Eximbank has an estimated \$7 billion in excess program authority over this period: \$5 billion in guarantees (\$2.0 billion in FY 83 and \$3.0 billion in FY 84) and \$2.0 billion in direct credits (FY 83 only). If extraordinary direct credit financing is used extensively, however, the Administration may have to seek supplemental direct credit authority in FY 84. CCC's FY 84 \$3.0 billion guarantee ceiling may not be adequate to meet anticipated demands for extraordinary financing. However, its specific export financing program budget level can be adjusted by Administration action. Rough estimates -- based on past years' experience and projected demands from countries experiencing serious financial problems -- indicate that extraordinary demand for CCC guarantees, might be \$2.4 billion, some portion of which could be accommodated within CCC's current \$3.0 billion ceiling.<sup>15</sup>

<sup>15/</sup> OMB believes that the substantial excess capacity available in Eximbank's programs could be used to support agricultural exports, thereby reducing demand for additional CCC authority.

CONFIDENTIAL

CONFIDENTIAL

-- 41 --

Cost/Benefit. The major cost of using Eximbank and CCC programs to offer debt relief is that it tends to undermine the commercial nature of these programs. Moreover, unlike aid programs, both Eximbank and CCC must be satisfied that there is a reasonable assurance of repayment before approving a transaction. To ensure that the debtor country is taking steps to improve its economic situation, thereby maximizing prospects for repayment, the provision of these extraordinary financing facilities should be linked to a number of explicit, but flexible conditions, according to individual country circumstances. These include:

(1) The government of the recipient country should provide its full and credit guarantee.

(2) The facilities should be specifically linked to continued commercial bank financing and might be used as an incentive for commercial banks to participate in their fair share in new lending to each country.

(3) Other governments should provide new credits along with the increase in U.S. credits to assure equitable sharing of the financing burden.

(4) The new credits should be provided only to countries with IMF stabilization programs and which stay in compliance with them.

(5) Any pending or impending debt rescheduling arrangements would normally form an integral part of such extraordinary financing.

The major benefits of a coordinated and comprehensive extraordinary financing arrangement are that it (1) assures access to credit for the debtor country so it can continue to import priority goods, (2) attracts additional commercial bank financing, and (3) assists successful implementation of domestic adjustment programs.

The Trigger and Shape of the Program. The "trigger" presumption must be that an IMF adjustment program is in place, that its conditionality requirements are being met, or, if not, that there is an exceptional reason why not, and that extraordinary U.S. trade finance assistance is justified in the circumstances.

The shape of the extraordinary U.S. assistance package cannot be prejudged, but must reflect a decision on the specific needs of the country and the precise U.S. objectives for undertaking the program. They could, for example, include announcement of a program to reestablish financial market confidence, to target assistance to specific debtor country industrial product sectors, to provide vital agricultural inputs (such as

CONFIDENTIAL

CONFIDENTIAL

- 42 -

feedgrains or fertilizer), or to stimulate additionality in overall commercial bank lending in harmony with an IMF program.

Reserve Fund. While it is true that the volume of risky guarantees is likely to increase in FY 84, there is no real advantage for either Eximbank or CCC to create a reserve fund. When Eximbank faces an extraordinary claims situation, as it did in Mexico, claims would likely be put on the books as purchases of assets, and have no impact on the Bank's capital and reserves. Any claims not booked as purchases of assets can be paid by drawing on capital and reserves, which currently amount to almost \$3.0 billion. Ultimate claims recovery is difficult to estimate and is tied to country economic improvement. For CCC, the "reserve fund" is infinite since CCC has unlimited borrowing authority from Treasury. However, since CCC's outstanding borrowings are limited to \$25 billion, pay-outs not written off as losses (i.e., Congress has not appropriated new funds to enable CCC to repay Treasury), diminish CCC's borrowing ability for other purposes mandated by CCC's Charter.

Claims arising from extraordinary financing have a high probability of recovery, since they should be backed by the full faith and credit guarantee of the debtor country. Special reserve funds are a bit of a delusion, giving false comfort to those facing the decision of whether or not the financing is structured so as to provide a reasonable assurance of repayment.

Burdensharing. The U.S. Government is currently gathering information about the capabilities and policies of foreign creditor countries to give us a stronger position in negotiating burdensharing options with other creditors. Burdensharing formulas could, for example, be based on trade patterns or bank exposure, taking trade policy issues into account.

CONFIDENTIAL